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IN THE

Supreme Court of the United States

October Term, 1971

Docket No. 71-421

TEXAS GULF SULPHUR COMPANY and CHARLES F. FOGARTY,
Petitioners,

against

WALTER A. MITCHELL,
Respondent.

TEXAS GULF SULPHUR COMPANY and CHARLES F. FOGARTY,
Petitioners,

against

GEORGE GORDON REYNOLDS,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit

PETITIONERS' REPLY BRIEF

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Opinion Below

The decision below has now been officially reported at 446 F. 2d 80.

Introductory Statement

There appear to be discrepancies in the facts cited to this Court by petitioners and those contained in the Brief for Respondents in Opposition (hereafter "Res. Br.").

These discrepancies relate to the nature of Texas Gulf's press releases of April 12 and April 16, 1964 and the timing of respondents' sales of stock in relation to the second release. These apparent discrepancies are easily resolved by reference to stipulated or otherwise undisputed facts contained in the record below.

Respondents assert that "all the essential information" contained in Texas Gulf's press release of April 16, 1964 "was based upon exploration which had been completed prior to April 12, 1964", and that "a materially significant portion * * * had been available to TGS since November of 1963" (Res. Br., p. 4). The November information referred to was a single 1¼" drill core 655 feet in length, a description of which comprised part of the April 16 release (4a, 42a).

Facts stipulated by the parties show that the April 12 release, which contained no details of drilling results, was prepared at a time when the draftsmen of the release had available reports on 2,804 feet of drilling; when the April 16 release was prepared, reports on 5,257 feet of drilling were available. The dispute between the parties does not relate to what information was available, but rather what the law required Texas Gulf to say in light of that information when it commented on the rumors which were then circulating, and whether respondents have a claim for damages based on what was said.

Another discrepancy would appear to surround the timing of respondents' sales with respect to the availability of information contained in the April 16 release. It is un-

controverted that at approximately 8:00 A.M.* on April 16, 1964, that release was issued to the news media. It was stipulated that at 8:29 A.M. the brokerage firm used by Reynolds in Utah received a teletype reporting Texas Gulf's announcement of a major discovery. It was stipulated that a Dow-Jones news wire appeared on the broad tape in all brokerage houses in the country by 8:55 A.M., announcing a major discovery of 25,000,000 tons of ore, and that a supplement to that report had been received by 9:02 A.M.

Mr. Reynolds testified that at 8:45 A.M. or 9:00 A.M. on April 16 his broker called and advised him of a rumor that Texas Gulf had made a big strike. The brokerage house record revealed that Mr. Reynolds' order to sell was placed in Salt Lake City at 9:10 A.M. When the first order could not be consummated, Reynolds and his broker spoke again, and a second order was placed at 9:23 A.M., and the transaction closed at 9:31 A.M.

It was stipulated that Mitchell's first order was placed at 12:40 P.M., some three and one-half hours after his Los Angeles brokers received and posted the Dow-Jones announcement of Texas Gulf's discovery. His order to sell was placed several points above the then market, and could not be consummated until the following day when his specified price was first reached upon the stock exchange auction market.

There may be a dispute as to whether these respondents actually knew about the April 16 release when they sold. But stipulated facts fix the availability of that information to both of them well before either sale order was placed,

* All times referred to are Mountain Standard Time.

and the petitioners' contentions do not in any degree turn upon any "time lag between when the sale order was delivered and when trades were technically negotiated," as respondents suggest (Res. Br., p. 5). See Petition, pp. 23-24.

Discussion in Reply

A.

Respondents state that the petition presents no important questions which merit review by this Court. Their position is premised upon the proposition that the questions here raised will be decided by this Court in its consideration of *Manhattan Casualty Co.* v. *Bankers Life & Casualty Co.*, Docket No. 70-60 (Oct. Term, 1971) and *Affiliated Ute Citizens* v. *United States,* Docket No. 70-78 (Oct. Term, 1971).* This is simply not the case. While both of those appeals present significant questions with respect to the interpretation and application of Rule 10b-5, neither presents the wide range of issues nor has the far-reaching significance and consequences of this case and the companion case of *SEC* v. *Texas Gulf* (Docket Nos. 327, 328, 346, 347).**

Both *Manhattan Casualty* and *Affiliated Ute Citizens* involved schemes to defraud, schemes designed to benefit the defendants at the expense of the particular plaintiffs. The instant case involves the issue of liability of a cor-

* The Circuit Court decisions in these cases are reported at 430 F.2d 355 (2d Cir. 1970) and 431 F.2d 1349 (10th Cir. 1970).

** We urge that this Court consider this petition in conjunction with the petitions in the *SEC* action. Both cases involve the same factual setting, and several of the legal principles first announced in the *SEC* case were applied by the Tenth Circuit below within a different legal context. The Solicitor General's Brief in *SEC* v. *Texas Gulf* is scheduled to be filed by November 8, 1971.

poration and its officers to potentially thousands of persons with whom they had no business dealings, and from whom they took no property and acquired no benefit. The present case does not arise from a scheme to defraud anyone, but rather from an attempt with laudable motives to warn the public of extravagant rumors.

The present case and the *Manhattan Casualty* and *Affiliated Ute Citizens* cases do involve the same administratively promulgated regulation, and some of the same clauses of that regulation, particularly the requirement that the fraud be "in connection with the purchase or sale of any security." But there the similarity ends. *Manhattan Casualty* presents the questions of whether a person must be a purchaser or seller of securities to maintain a private action under Section 10(b) and Rule 10b-5, and whether the "in connection with" requirement is satisfied when the scheme is to loot the assets of the corporation and the proceeds of a sale of securities are diverted, where neither the purchaser nor the seller was deceived in the securities transaction. The question under Rule 10b-5 (as distinct from questions under the Indian statute) presented in *Affiliated Ute Citizens* v. *United States* involves the liability of persons aiding or abetting persons benefiting in a fraudulent securities transaction, although not themselves purchasing. Neither case presents the broad and important questions of *scienter,* reliance, causation, damages and statute of limitations here present, nor the broad and basic policy issues involved in the publication of information of interest to business, stockholders and the public at large by a company which is not dealing in or attempting to influence the price of securities. It would be in the public interest for the Court to address itself at this time not only

to the important questions presented in the *Manhattan Casualty* and *Affiliated Ute Citizens* cases, but also to the far broader questions presented in this case and in *SEC* v. *Texas Gulf*.

Respondents further contend that the thrust of this petition for certiorari is to suggest that this Court should import restrictive provisions of other securities laws into Rule 10b-5, and that to do so "would emasculate the intent of Congress." While Congress expressly provided private rights of action under the statutes referred to by respondents (Res. Br., p. 6), a private right of action under Section 10(b) and Rule 10b-5 was not so provided, and that right of action has been judicially created by the lower federal courts. The elements which must be proved in establishing a private right of action not created by Congress is the issue before this Court.

The statute and rule as drafted are predicated upon "manipulative and deceptive devices" and "fraud and deceit." Rather than suggesting the addition of restrictions from other sections of the securities laws, petitioners' position is that the statutory and regulatory language should be given its clear meaning, and that in order to recover damages under Rule 10b-5, a plaintiff should be required to prove intentional or knowledgeable wrongdoing in connection with a securities transaction, and that some of the elements of an action for fraud or deceit are present; that is, there was at least a false representation of a material fact made with intent to deceive, upon which plaintiff reasonably relied and was caused damage thereby. These elements are incorporated into the securities law provisions to which petitioners referred, evidencing the intent of Congress that liability would not be unlimited. Dispensing with

these basic elements as respondents suggest would effectively negate Congressional intent expressed in the carefully drawn legislation.

B.

The precedents cited by respondents to support jurisdiction over Dr. Fogarty in the District of Utah (Res. Br., p. 7) do not reach the question here presented. Each of those cases involved deliberate use by the defendant of facilities within the forum state in the course of a securities transaction. Dr. Fogarty engaged in no such purposeful activity within Utah as the Constitution requires.

C.

Respondents also argue that the question of the measure of damages should not be reviewed by this Court, that it is not a question of national importance. Yet it can affect the financial viability of corporations in every state in this nation.

With the burgeoning increase of Rule 10b-5 suits and class actions,* the question of damages to be awarded is of importance to the management of every publicly-held corporation which may conceivably be called upon to issue a press release on a matter of importance to shareholders or to the public, and to other corporations, accountants, and

* Indeed, this Court has been advised not only that respondents will separately petition this Court for review of the treatment of this case as a class action (Res. Br., pp. 5-6, n.), but also of the pendency of another class action involving Texas Gulf's press release. The Tenth Circuit noted that if its damage measure were adopted, liability could amount to millions of dollars (66a-67a n.). Just the differential between the damage measures applied below by the District Court and the Court of Appeals can in a class action mount into the millions, and it alone presents to this Court a question requiring review.

businessmen, etc., caught up in the myriad of charges brought under Rule 10b-5. This question is of equal importance to investors everywhere who could find themselves paying monumental judgments through their ownership of stock in a defendant corporation. The investments of one group of shareholders, who retained their stock in the company, are depleted by payments to identically situated shareholders who sold, even though the corporation or its shareholders did not receive and did not intend any benefit from the corporate action.

The authorities cited by respondents on the damage issues are not in point. This is neither a case of conversion (*Galigher* v. *Jones,* 129 U.S. 193 (1889)), nor a case where defendants reaped profits which should in justice be returned to plaintiff (*Janigan* v. *Taylor,* 344 F.2d 781 (1st Cir.), *cert. denied,* 382 U.S. 879 (1965)). Texas Gulf did not profit from the issuance of the April 12 release; and respondents received for their stock the prevailing market price reflecting the judgment of the investing public following issuance of Texas Gulf's April 16, 1964 release. Respondents received for their stock higher prices than obtained prior to the issuance of the press release of which they complain. The Securities Exchange Act provides only for the recovery of "actual damages" (15 U.S.C. §78bb (a)); here respondents suffered none.

D.

In *Charney* v. *Thomas,* 372 F.2d 97 (6th Cir. 1967) (Res. Br., p. 9), the Sixth Circuit Court of Appeals observed that "in some cases the local Blue Sky Law might be the more appropriate point of reference", but that in that

case Michigan law contained "no provision similar to section 10(b) of the federal law." *Id.* at 100. Thus the court applied Michigan's fraud statute of limitations. But Utah's Blue Sky provisions contain language almost identical to Rule 10b-5, and if the elements of fraud are to be dropped from Rule 10b-5 actions, fraud statutes of limitations have no applicability. The conflict of the decision below with *Vanderboom* v. *Sexton,* 422 F.2d 1233 (8th Cir.), *cert. denied,* 400 U.S. 852 (1970), also warrants review.

Conclusion

It is respectfully requested that this petition for a writ of certiorari be considered in conjunction with the companion petitions in *SEC* v. *Texas Gulf Sulphur* (Docket Nos. 327, 328, 346, 347), and that all such petitions be granted for the reasons set forth therein.

Respectfully submitted,

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